INDIANA CHARTER SCHOOL HANDBOOK

Indiana Public Charter Schools Association

The Legal Issues in Forming A Charter School

October 7, 2011

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First printing in 2011

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INTRODUCTION

Indiana first enacted charter school enabling legislation in 2001, and, as of the Fall of 2011, there were 61 charter schools operating in the state. On May 5, 2011, the Governor of Indiana signed into law House Enrolled Act 1002 significantly expanding access to charter schools across the state. Among other changes, HEA 1002 increases the number of charter school authorizers, creates a new statewide body (the Indiana Charter School Board) that can issue charters, gives charters more flexibility to hire non-traditional educators and part-time teachers, gives charters more access to unused facilities owned by traditional public schools and allows for conversion of an existing public school to a charter school under certain conditions. As a result, it is expected that between 20-30 new charter schools will open in Indiana in the next 5 years.

You may be reading this guide because you have been asked to be on the board of a new charter school – or the charter school board upon which you serve has or will be undertaking a retreat, strategic planning process, or other significant undertaking that requires your active engagement – or your board leadership has sent this to you and your fellow board members as an educational piece. Whatever the reason, congratulations! You are likely part of or being recruited into a well-functioning organization that takes the role of its board seriously enough to seek your engagement.

At Ice Miller LLP, we take the role of charter school board members seriously. We developed this handbook that outlines your roles and responsibilities, the legal requirements for your organization, the protections afforded you in your role as a director of a nonprofit charter school, and what you, in turn, should expect from your organization.

Both the nonprofit and charter school sectors have evolved throughout the years, becoming more complex, sophisticated and regulated. This is particularly true in the charter school context, as in addition to the state rules applicable to nonprofit corporations and the federal rules applicable to tax-exempt entities, charter schools have additional layers of regulation by and accountability to their authorizers and to the public.

In Indiana, your board duties require you to act in good faith, with the care of an ordinarily prudent person, and in a manner you reasonably believe to be in the best interests of the organization. In addition to a working familiarity with the mission of your school, you also should have a basic knowledge of what a nonprofit, tax-exempt charter school may do, what they may not do, and how they differ legally, structurally and operationally from commercial enterprises.

Our hope is that this handbook will assist you in your ongoing efforts to be a diligent, thoughtful, faithful and informed resource to the school that you serve and, in so doing, enable you and your school to make the most of your service.

HOW TO USE THIS BOOK

This handbook is intended to be a resource to you. Each chapter provides a general overview of a particular issue or general topic of interest to a charter school which is both an Indiana nonprofit corporation and an organization that is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the "Code"). We hope that the information in this handbook enables you to spot issues, to recognize the need to obtain additional information when it arises, and to ask good questions so that you may receive good answers. However, please realize that the information provided is by no means an exhaustive discussion. When a situation arises that causes you concern based on the general information provided in this handbook, you should consult with an objective legal advisor who is knowledgeable regarding nonprofit and tax-exempt issues as they relate to charter schools.

CHAPTER 1

INDIANA CHARTER SCHOOLS

What Is A Charter School?

An Indiana charter school is defined as a nonsectarian and nonreligious public school that operates under a contract or charter with a charter school sponsor.[1] Under Indiana law, a charter school may be established to provide "innovative and autonomous" programs that do any of the following: (1) serve the different learning styles and needs of public school students; (2) offer public school students appropriate and innovative choices; (3) provide varied opportunities for professional educators; (4) allow public schools freedom and flexibility in exchange for exceptional levels of accountability; and (5) provide parents, students, community members, and local entities with an expanded opportunity for involvement in the public school system. A charter school must be open to any student who resides in Indiana and may not establish admission policies or limit student admissions in any manner in which a public school is not permitted to establish admission policies or limit student admissions.[2]

A charter school is formed when a charter school sponsor grants a charter to an organizer to operate a charter school. A charter school "organizer" may be any group or entity that has been determined by the Internal Revenue Service ("IRS") to be operating as a tax-exempt charity (e.g., that is exempt under Code Section 501(c)(3)) or has applied for such determination, and whose organizational documents include a provision that upon dissolution all of its remaining assets must be used for nonprofit educational purposes.[3] A sponsor may not grant a charter to a for profit organizer. A charter school "sponsor" means one of the following: a governing body;[4] a state educational institution that offers a four year baccalaureate degree; the Mayor of Indianapolis; the Indiana Charter School Board; and a nonprofit college or university that provides a four year educational program for which it awards a baccalaureate or more advanced degree. There are currently two sponsors actively accepting charter school applications: the Indianapolis Mayor's Office of Education Innovation and the Ball State University Office of Charter Schools. A third, the newly created Indiana Charter School Board, expects to sponsor its first charter schools for the 2012 – 2013 school year.[5]

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[1] Indiana's Charter School law can be found at Indiana Code ("IC") 20-24-1, *et. seq.*

[2] A charter school is permitted to operate as a single gender school if approved to do so by a sponsor. IC 20-24-54(b).

[3] Other than funds received from the Indiana State Department of Education ("DOE") which must be returned to the DOE.

[4] A "governing body" means: (1) a township trustee and the township board of a school township; (2) a county board of education; (3) a board of school commissioners; (4) a metropolitan board of education; (5) a board of trustees; or (6) any other board or commission charged by law with the responsibility of administering the affairs of a school corporation. IC 20-18-2-5.

[5] There are also two "governing bodies" acting as charter school sponsors: Evansville-Vanderburgh School Corporation (2 schools) and Lafayette School Corporation (1 school). However, neither school corporation is actively accepting charter school applications.

A charter school may be either a nonconversion or a conversion charter school. A nonconversion charter school is a newly created public elementary or secondary school. A conversion charter school is a charter school that is established by converting an existing public elementary or secondary school into a charter school. An existing public elementary or secondary school may be converted into a charter school if: (1) at least fifty-one percent of the parents of students who attend the school have signed a petition requesting the conversion, (2) the school has been placed in either of the two lowest categories or designations of "school improvement" for two consecutive years, and (3) the governing body votes to convert the school.

A charter school may: (1) sue and be sued in its own name; (2) acquire real and personal property or an interest in real and personal property by purchase, gift, grant, devise, or bequest for educational purposes; (3) convey property; and (4) enter into contracts in its own name, including contracts for services. A charter school may not: (1) operate at a site or for grades other than as specified in the charter; (2) charge tuition to any student residing within the school corporation's geographic boundaries (other than for a preschool or latch-key program); (3) enroll a student who is not a resident of Indiana (other than foreign exchange students); (4) be located in a private residence; or (5) provide solely home based instruction.

What is a Charter?

A charter is a written contract between a charter school organizer and a sponsor for the establishment of a charter school. The charter confers certain rights, franchises, privileges, and obligations on a charter school and confirms the status of the charter school as a public school. A charter must be granted for a fixed number of, but no less than three, years and must specify the grounds under which the sponsor may revoke the charter before the end of its term and under which a charter will not be renewed.

Application of State and Federal Laws to Charter Schools

A charter school, including a private school that becomes a charter school, is required to follow all applicable federal, state, and local laws, rules and guidelines. The school must have open enrollment policies and cannot discriminate based on disability, race, color, gender, national origin, religion, or ancestry.

Furthermore, as a charter school is considered to be an Indiana public school, many of the laws applicable to public schools are also applicable to charter schools, including, but not limited to: required financial audits by the state board of accounts, student health and safety laws, compulsory school attendance laws, and accountability laws.[6] Furthermore, a charter school must make Adequate Yearly Progress under the federal No Child Left Behind Act of 2001, charter school students must take the ISTEP+ exam, and a charter school's curriculum must meet

[6] For a complete list of the state laws that apply to charter schools, see Appendix A.

Indiana's academic standards. Like a traditional public school, a charter school is assessed for ISTEP+ performance and improvement and is placed in categories for Indiana Public Law 221.[7]

However, Indiana charter schools are exempt from those Indiana laws not specifically listed as applicable to charter schools. Charter schools are also exempt from rules or guidelines adopted by the Indiana state board of education, rules and guidelines adopted by the professional standards board (except for rules regarding gaining or renewing a teacher's license) and regulations or policies adopted by a school corporation. As public schools, charters are subject to the state disclosure and access laws applicable to all public agencies, such as the Indiana Open Door Law and the Access to Public Records Act, discussed in more detail in *Chapters 7* and *8*.

Charter School Accountability

The sponsor of a charter school is primarily responsible for school oversight and ensuring that the school complies with applicable state and federal laws and the terms of its charter. A sponsor is required by statute to review a charter school's performance in achieving its academic goals at least once for each five year period in which the charter is in effect. Furthermore, a charter school is required to regularly provide to its sponsor attendance records, student performance data and financial information and to develop a school improvement plan, and are assessed on their progress in certain areas. Charter schools are required to set annual performance targets in conjunction with the sponsor that are designed to help the school to meet applicable federal, state and sponsor expectations, including, but not limited to: (i) required state assessment measures (e.g., the Indiana Statewide Testing for Educational Progress Plus (ISTEP+) program and End-of-Course Assessments); (ii) attendance and graduation (if appropriate) rates; (iii) the numbers of Core 40 diplomas and other college and career ready indicators (e.g., advanced placement, dual credit and International Baccalaureate participation and passage) (if appropriate); (iv) the numbers of academic honors and technical honors diplomas (if appropriate); (v) student academic growth; (vi) financial performance and stability; and (viii) governing board performance and stewardship, including compliance with applicable laws, rules and regulations. Like public schools, charter schools are placed in school improvement and performance categories based on assessment results.

A sponsor may revoke a charter at any time before the expiration of the term of the charter if: (1) the organizer fails to comply with the conditions established in the charter; (2) the charter school established by the organizer fails to meet the educational goals set forth in the charter; (3) the organizer fails to comply with all applicable laws; or (4) the organizer fails to meet generally accepted government accounting principles.

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[7] Public Law 221 (P.L.221) is Indiana's comprehensive accountability system for K-12 education. Passed by the Indiana General Assembly in 1999, prior to the No Child Left Behind Act, the law aimed to establish major educational reform and accountability statewide. P.L.221 places Indiana schools (both public and accredited non-public) into one of five categories based upon student performance and improvement data from the state's ISTEP+ and End-of-Course Assessments.

CHAPTER 2

INDIANA NONPROFIT CORPORATIONS

As previously discussed, a charter school organizer may be any group or entity that has been determined by the IRS to be operating as a tax-exempt charity (e.g., that is exempt under Code Section 501(c)(3)) or has applied for such determination, and whose organizational documents include a provision that upon dissolution all of its remaining assets must be used for nonprofit educational purposes. An organizer must therefore be organized as an Indiana nonprofit corporation.

Qualification as a Nonprofit Corporation under the 1991 Act

First, it is important to understand that a nonprofit corporation is not necessarily a tax-exempt organization. Nonprofit corporations may be either taxable or tax-exempt. A nonprofit corporation is exempt from tax only if it complies with the requirements for exemption under Code Section 501(a).

The Indiana Nonprofit Corporation Act of 1991, as amended (the "1991 Act"), is contained in Indiana Code Section 23-17 and sets forth the state law requirements for status as a nonprofit corporation in Indiana. The 1991 Act places all nonprofit corporations into one of three categories based on the corporation's goals: (1) public benefit, (2) religious, or (3) mutual benefit. A public benefit corporation is organized for public or charitable purposes and generally includes those organizations recognized as tax-exempt under Code Section 501(c)(3). To be classified as a public benefit corporation, the corporation must not be a religious organization and must include in its Articles of Incorporation a statement that its assets will be distributed to an organization organized for public or charitable purposes, a religious corporation, the United States, a state, or a Code Section 501(c)(3) organization. A religious corporation is organized primarily or exclusively for religious purposes or is designated a religious corporation under federal law. A mutual benefit corporation is a corporation that is not a public benefit or religious corporation.

Articles of Incorporation

An Indiana nonprofit corporation is formed by filing Articles of Incorporation with the Indiana Secretary of State, accompanied by a $30 filing fee. This is a public document and, therefore, generally contains only basic information regarding the corporation and its operations. Indiana law requires that certain items be included in a nonprofit corporation's Articles of Incorporation, such as the name of the corporation (which must include the word "corporation," "incorporated," "company," "limited," or an abbreviation of one of the foregoing), a statement of classification (i.e., that it will be a public benefit corporation), the name and address of the incorporator and whether the corporation will have members. The Articles of Incorporation may also include items such as the corporation's purpose, the names and addresses of the initial

directors of the corporation, and any other provision that is required or allowed to be set forth in the Bylaws.

Bylaws

An organization's Bylaws are a companion document to the Articles of Incorporation and generally contain more detailed provisions regarding the governance of the corporation. The Bylaws are a private document and are not filed with any state office.

Members

A nonprofit corporation is not required to have members under Indiana law. If it does, the members may be admitted pursuant to any criteria or procedure established in the Articles of Incorporation or Bylaws. Members do not have to pay a fee or dues or provide any other type of consideration to be admitted to the corporation's membership unless the Articles of Incorporation or Bylaws provide otherwise. By definition, members with voting rights have a right to vote on the election of directors, amendment of the Articles of Incorporation, adoption of a plan of merger, the sale of all or substantially all of the corporation's assets, and the dissolution of the corporation. In fact, Indiana law requires approval by the members of a corporation before any of the aforementioned actions may be taken. Classes of members are permitted.

Member meetings. A corporation with members must hold an annual membership meeting at a time stated in or fixed in accordance with the Bylaws. At that meeting, the president and treasurer must report on the activities and financial condition of the corporation. Regular meetings of the membership may be held at the times stated or fixed in the Bylaws. Special meetings must be held on the call of the president, the board of directors, or any other person authorized by the Articles of Incorporation or Bylaws or by the holders of 10% of member votes entitled to be cast at the meeting. A member may participate in meetings by or through the use of a telecommunications device (e.g., conference call) unless the Articles of Incorporation or Bylaws of the corporation provide otherwise.

Notice of a meeting of the members is valid if it is "fair and reasonable." Generally, notice will be considered to be fair and reasonable if it is given not less than 10 days (30 days if mailed other than by first class or registered mail) but not more than 60 days before the meeting date stating the place, date and time of the meeting. If the meeting is a special meeting, the meeting notice must include a description of the meeting's purpose. If the organization has more than 1,000 members, it is sufficient to publish notice of the meeting in a newspaper of general circulation 10 to 30 days before the meeting date. Notice may be waived by a member in certain circumstances. As a charter school is considered to be a public agency, member meetings of a charter school organizer are subject to the Indiana Open Door Law requirements, discussed in further detail in *Chapter 7*.

Voting. Quorum for a members' meeting under Indiana law is 10% of the votes entitled to be cast (represented in person or by proxy), but the Articles of Incorporation or Bylaws can provide for a higher or lower quorum. If the matter to be voted on is not described in the meeting notice, the quorum is increased to 33 ⅓%. Action may be taken by written ballot in lieu

of a meeting. Alternatively, action may be taken by written consent in lieu of a meeting if the action is approved by at least 80% of the votes entitled to be cast on the action and consent is delivered to the corporation for inclusion in the minutes. The Articles of Incorporation or Bylaws can alter the foregoing requirements.

Directors

A board of directors must consist of at least three individuals. Directors may be elected, designated or appointed. While the term of an elected director may not exceed five years, there is no limitation on the term of a designated or appointed director. Directors who are elected by the members may be removed by the members, with or without cause, unless the Articles of Incorporation or Bylaws provide otherwise.

Meetings. Notice to board members is not required for regular meetings but is required for special meetings. Notice of the date, time and place of a special meeting is required at least two days prior to the meeting. The notice does not need to describe the purpose of the special meeting. A special meeting may be called by the presiding officer of the board of directors, the president or 20% of the directors then in office, unless the Articles of Incorporation or Bylaws provide otherwise. Notice can be waived by a written waiver or by attendance. A director may participate in a meeting through the use of a telecommunications device unless the Articles of Incorporation or Bylaws provide otherwise. Meetings of a charter school board are also subject to the Indiana Open Door Law requirements.

Voting. A quorum of the board of directors consists of a majority of the directors in office immediately before a meeting begins. The Articles of Incorporation or Bylaws can alter this quorum requirement. However, neither document may authorize a quorum of fewer than: (a) 1/3 of the number of directors in office; or (b) 2 directors, whichever is greater. Action may be taken by unanimous written consent.

Committees. To exercise board powers, a committee must:

- Be created by the board of directors by a majority vote (or the vote otherwise required for board action, if greater);
- Be composed entirely of directors appointed by the board by a majority vote (or the vote otherwise required for board action, if greater); and
- Consist of at least two directors.

The committee may exercise the authority of the board of directors to the extent specified in the Articles of Incorporation or Bylaws. However, a committee cannot perform certain actions, such as authorizing distributions, approving or recommending to the members dissolution, merger, or sale of the corporation and adopting, amending or repealing the Articles of Incorporation or Bylaws.

CHAPTER 3

FEDERAL TAX-EXEMPTION UNDER CODE SECTION 501(C)(3)

Charter Schools as 501(c)(3) Organizations

An organization will be classified as a charitable organization that is exempt from federal income tax if: (1) the purpose and nature of its activities are "charitable," and (2) it does not unduly benefit private interests. While Code Section 501(c)(3) allows exemption for a number of different types of entities,[8] a charter school will most often qualify for exemption as an "educational" organization under Code Sections 509(a)(1) and 170(b)(1)(A)(ii). This charitable designation is generally limited to educational organizations that maintain a regular faculty and curriculum and have a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. A formal schedule of classroom instruction is not strictly required.[9] A charter school organizer may also qualify under the "charitable" classification as an organization formed to relieve the poor and distressed or the underprivileged, to advance education, to lessen neighborhood tensions or to combat community deterioration and juvenile delinquency.

Tests for Qualification

An organization must meet both the organizational test and the operational test contained in Treasury Regulation § 1.501(c)(3)-1 in order to qualify as a tax-exempt organization under Code Section 501(c)(3).

Organizational Test

In order to satisfy the organizational test, an exempt organization's governing documents must: (1) limit the organization's purposes to one or more exempt purposes; (2) not expressly empower the organization to engage in non-exempt activities; and (3) provide that, upon dissolution, its assets will be distributed for one or more exempt purposes. If the entity is "organized" to devote more than an "insubstantial" amount of activities to influence legislation or to act directly or indirectly to influence political campaigns, it will not qualify for exempt status.

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[8] *E.g.*, religious, charitable (relief of the poor and distressed or of the underprivileged; advancement of education; lessening the burdens of government; lessening neighborhood tensions; eliminating prejudice and discrimination; and combating community deterioration and juvenile delinquency), scientific, testing for public safety, literary, educational, fostering amateur sports competition; and prevention of cruelty to children or animals.

[9] Rev. Rul. 72-430, 1972-2 C.B. 105.

Operational Test

Under the operational test, an entity's activities must further public, rather than private, purposes. The amount and extent of an organization's "charitable" activities are weighed against its social or other non-exempt activities. Thus, if an organization performs a substantial part of its activities to further a non-exempt purpose, it will fail the operational test. In addition, an organization will not be regarded as exempt if: (1) its net earnings inure in whole or in part to private individuals; or (2) a substantial part of its activities are used to influence legislation.

Private Inurement

The private inurement doctrine provides that a tax-exempt organization may not be operated for the benefit of private individuals. An organization's net earnings may not inure to the benefit of individuals who control the organization (e.g., shareholders, creators, directors). The concern is whether substantial benefits inure to private individuals who created or are involved in the organization (i.e., "insiders").

Code Section 4958 imposes a tax on any disqualified person who engages in an excess benefit transaction with a public charity. These taxes, discussed in further detail in *Chapter 10*, are commonly referred to as "intermediate sanctions" because they provide the IRS with a sanction short of revoking the tax-exempt status of an organization that has engaged in private inurement.

Private Benefit

Even when an organization does not allow earnings to inure to the benefit of "insiders," the organization must operate in a manner that does not benefit any particular private class of persons. The private benefit doctrine applies to groups of individuals that may not be "insiders." The prohibition against private benefit extends to "disinterested persons," as distinguished from shareholders or individuals having a personal and private interest in the organization.

Under the private benefit doctrine, the groups that benefit from the charitable organization: (1) must be members of a charitable class, and (2) must not comprise a select group of members earmarked to receive benefits. To be members of a charitable class, the groups must possess charitable characteristics (e.g., poor, underprivileged, educational, religious, etc).

Legislative Activity

To qualify for and maintain tax-exempt status, a substantial part of an organization's activities may not consist of attempting to influence legislation by propaganda or otherwise. Thus, a substantial part of an organization's activities may not include: (1) contacting or urging the public to contact legislators for the purpose of supporting or opposing legislation, or (2) advocating the adoption or rejection of legislation.

A Code Section 501(c)(3) organization that plans to engage in legislative activity should consider making a Code Section 501(h) election. As opposed to the vagueness provided by the

above test, Code Section 501(h) sets specific dollar limits on the amount that Code Section 501(c)(3) organizations may spend to influence legislation without incurring penalty taxes or losing their exempt status. Code Section 501(h) also provides clear definitions of what constitutes lobbying. The Code Section 501(h) election is made on Form 5768.

Political Activity

A tax-exempt organization may not participate or intervene, directly or indirectly, in any political campaign for or against any candidate to public office. Unlike legislative activity, which can be conducted by an exempt organization within limits, an organization will jeopardize its tax-exempt status if it participates or intervenes in a political campaign with respect to a candidate for public office.

Application Process for Code Section 501(c)(3) Organizations

An organization that wants to be classified as an organization described in Code Section 501(c)(3) must apply to the IRS for recognition of such status on Form 1023. In general, if an organization files its application within 27 months after the end of the month in which it was formed and the IRS approves the application, the effective date of the organization's Code Section 50l(c)(3) status will be the date it was organized.

Application Process for Indiana Sales Tax Exemption

An Indiana nonprofit organization is exempt from income tax in Indiana unless it has income which qualifies as unrelated business taxable income for federal purposes. If the organization wishes to be exempt from Indiana sales tax, it must file Form NP-20A to request such exemption. Form NP-20A is much less detailed than the federal Form 1023 but generally must be filed within 120 days of the organization's formation. Certain attachments to Form NP-20A may be required, such as a copy of the corporation's Articles of Incorporation and Bylaws. The Indiana Department of Revenue generally will not grant exemption until the organization can provide a copy of its federal determination letter.

CHAPTER 4

ONGOING FILING REQUIREMENTS

Annual Federal Filing Requirements

Annual Federal Filing Generally

Most tax-exempt charter schools are required to file an annual Form 990 or 990-EZ with the IRS.[10] A charter school that fails to file an annual return as required for 3 consecutive years, automatically loses its tax-exempt status.

Form 990, Return of Organization Exempt From Income Tax

This form is used by tax-exempt organizations to provide the IRS with the information required by Code Section 6033, including the gross income, receipts and disbursements of the organization. For tax years beginning with 2010, an organization with annual gross receipts of greater than or equal to $200,000 or total assets greater than or equal to $500,000 is required to file this form. Form 990, if required, must be filed by the 15th day of the fifth month following the close of the tax year.

Form 990-EZ, Short Form Return of Organization Exempt From Income Tax

For tax years beginning with 2010, an organization may file this form instead of Form 990 if its annual gross receipts are greater than $50,000 and less than $200,000 and its total assets at the end of the year are less than $500,000. This form, if used, must be filed by the 15th day of the fifth month following the close of the tax year.

Form 990-T, Exempt Organization Business Income Tax Return

This form is used for determining and reporting gross income from an unrelated trade or business (see *Chapter 11* for a further discussion of such income). Form 990-T is required only if an organization receives unrelated business taxable income in excess of $1,000 per year. This form must be filed by the 15th day of the fifth month following the close of the tax year.

Form 4720, Return of Certain Excise Taxes on Charities and Other Persons Under Chapters 41 and 42 of the Internal Revenue Code

Form 4720 is used to report the Code Section 4958 initial taxes on disqualified persons and organization managers of Code Section 501(c)(3) and Code Section 501(c)(4) organizations

[10] In addition, an organization whose gross receipts are normally $50,000 or less is generally required to file Form 990-N (e-Postcard) electronically by the 15th day of the fifth month following the close of the tax year.

that engage in excess benefit transactions. Furthermore, Form 4720 is used to: (1) report the Code Section 4911 tax on excess lobbying expenditures by public charities that have elected to be subject to Code Section 501(h) regarding expenditures to influence legislation; (2) report the Code Section 4912 tax on excess lobbying expenditures that result in loss of tax-exempt status; (3) report the Code Section 4055 tax imposed on any amount paid or incurred by an exempt organization that participates or intervenes in any political campaign on behalf of, or in opposition to, any candidate for public office; and (4) report the Code Section 170(f)(10) tax on any premiums paid on a personal benefit contract in connection with a transfer to an organization or charitable remainder trust for which a transferor is disallowed a charitable deduction.

The organization is required to file this form only if it is required to pay any of the aforementioned taxes. Form 4720 must be filed by the due date for filing the organization's Form 990 or Form 990-EZ.

Annual Indiana Filing Requirements

Form NP-20, Indiana Nonprofit Organization's Annual Report

This annual state information tax return is required of all Indiana nonprofit corporations and must be filed by the 15th day of the fifth month following the close of the tax year. Form NP-20 requires only basic information with respect to the nonprofit corporation, such as its charitable purposes and whether any changes have been made to its Articles of Incorporation or Bylaws. A copy of the organization's Form 990 or 990-EZ must be attached to Form NP-20 if the organization is filing one of these federal forms for the tax year at issue.

Form IT-20NP, Indiana Nonprofit Organization Unrelated Business Income Tax Return

Form IT-20NP must be filed by a nonprofit corporation in addition to Form NP-20 if it has unrelated business income that is greater than $1,000 for the relevant tax year. The form must be filed by the 15th day of the fifth month following the close of the tax year.

Form 48725, Indiana Business Entity Report

This form is the annual state information entity return. It is not a tax return. A nonprofit corporation must file Form 48725 each year with the Indiana Secretary of State in the anniversary month of incorporation, accompanied by a $10 filing fee. This form may also be completed online. Failure to file will eventually result in administrative dissolution.

Other Federal Reporting Requirements

Form 8282, Donee Information Return (Sale, Exchange or Other Disposition of Donated Property)

This form is used by donee organizations to report information to the IRS about dispositions of certain charitable deduction property made within three years after the donor contributed the property. Original and successor donee organizations must file Form 8282 if

they sell, exchange, consume, or otherwise dispose of (with or without consideration) charitable deduction property within three years after the date the original donee received the property. Form 8282 must be filed within 125 days after the date of the disposition of the property.

If a donor contributes an item of property or a group of similar items for which he or she claimed a deduction of more than $5,000, he is required to complete Section B of Form 8283, *Noncash Charitable Contributions*, have the property appraised, request an acknowledgment of the contribution from the donee charitable organization and file Form 8283 with his or her federal income tax return. The donor is required to provide the name of the donee organization on the form and a description (but not necessarily the value) of the donated property before asking the donee organization to sign the form. Form 8283 must be signed by an official authorized to sign the tax returns of the organization, or a person specifically designated to sign Form 8283. Once signed, the donee organization should retain a copy of the form so it has a record of the date of the gift and the property contributed, as the sale of the property identified in Section B within 3 years of receipt causes the donee organization to file Form 8282. Form 8282 does not need to be filed if (i) the donor signed a statement on Form 8283 indicating that the appraised value of a specific item listed as a part of a group of items in Section B was not more than $500; or (ii) if the property is consumed or distributed without consideration in fulfilling the organization's charitable purposes or function.

Form 8300, Report of Cash Payments Over $10,000 Received in a Trade or Business

Each person engaged in a trade or business who, in the course of that trade or business, receives more than $10,000 in cash in one transaction or in two or more related transactions must file Form 8300. Any transactions conducted between a payer, or its agent, and the recipient in a 24-hour period are related transactions. Form 8300 must be filed with the IRS and the Financial Crimes Enforcement Network by the 15th day after the cash was received, and a copy of each Form 8300 filed must be kept by the filing organization or individual for five years after the date it is filed. A transaction includes the purchase of property or services, the payment of debt, the exchange of a negotiable instrument for cash and the receipt of cash to be held in escrow or trust.

Forms 941, W-2, W-3, W-4, 1099-MISC, Reports of Payments to Employees and Independent Contractors

Whether paid to employees or independent contractors, almost all payments made by exempt organizations to individuals or unincorporated entities are reportable to the IRS. The annual Form W-2 is filed for employees, while Form 1099-MISC is filed for most other payments to independent contractors and other nonemployees. Form 941 is filed quarterly and is used to report social security, Medicare and income taxes withheld by an employer and social security and Medicare taxes paid by an employer.

Federal Public Inspection and Disclosure Requirements

Treasury Regulation § 301.6104(d)-1 provides that if a tax-exempt organization filed a Form 1023, it must make its application for tax exemption and its annual information returns available for public inspection without charge at its principal, regional and district offices during

regular business hours. The organization may have an employee present in the room during the inspection, but the individual inspecting the application or annual information returns must be allowed to take notes freely. A tax-exempt organization that does not maintain a permanent office must comply with the public inspection requirements by making the applicable documents available for inspection at a reasonable location of its choice. Such an organization must allow the public inspection within a reasonable amount of time of the request (normally not more than two weeks) and at a reasonable time of day. In lieu of allowing an inspection, the organization can mail copies of the documents to the person requesting them within two weeks of the request.

For disclosure purposes, the application for exemption includes Form 1023, all documents and statements the IRS requires an applicant to file with the forms, any statement or other supporting documentation submitted by an organization in support of its application, and any letter or any other document issued by the IRS regarding the application (such as the determination letter or questions from the IRS about the application). An organization does not need to disclose an application that the IRS has not yet recognized, an application filed before July 15, 1987 (unless the organization had a copy of the application on that date), or the name and address of any contributor to the organization.

The annual information return materials that must be available for public inspection include an exact copy of any return filed by the organization pursuant to Code Section 6033, including Forms 990, 990-EZ, 990-T and 1065. Any amended returns filed with the IRS and all schedules, attachments and supporting documents must also be made available.

Annual information returns must be made available for three years beginning on the date the return is required to be filed or is actually filed, whichever is later. In addition, an organization must provide free copies (other than charges for reasonable duplication and actual postage costs) of all or any part of the application or returns required to be made available for public inspection to any person who makes a request for a copy in person or in writing.[11]

For a discussion of the State disclosure requirements applicable to charter schools, see *Chapter 7*.

[11] Information returns for most nonprofit organizations are freely available online on GuideStar, at http://www.guidestar.org.

CHAPTER 5

DUTIES, LIABILITY AND PROTECTIONS OF NONPROFIT DIRECTORS

Primary Duties

The three primary duties of a director of an Indiana nonprofit corporation are: (1) the duty of care, (2) the duty of loyalty, and (3) the duty of obedience. The duty of care concerns the director's competence in performing directorial functions and typically requires him or her to use the care that an ordinarily prudent person would exercise in a like position and under similar circumstances. The duty of loyalty requires the director's faithful pursuit of the interests of the organization he or she serves rather than personal financial or other interests or those of another person or organization. The duty of obedience requires that a director act with fidelity, within the bounds of law generally, to the organization's mission as expressed in its Articles of Incorporation and Bylaws.[12]

Duty of Care

Indiana Code Section 23-17-13-1, *et. seq.*, of the 1991 Act codifies a director's duty of care. A director of a nonprofit corporation must discharge his or her duties in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner in which the director reasonably believes to be in the best interest of the organization. At a minimum, a director should read minutes, attend meetings, listen and ask good questions.

In discharging the director's duties, a director may rely on information, opinions, reports, or statements, including financial statements and other financial data, if prepared or presented by a qualified professional whom the director reasonably believes to be reliable and competent in the matters presented. However, a director does not act in good faith if the director has personal knowledge concerning a matter which makes his or her reliance on such information unwarranted.

A director is not liable for an action taken as a director, or failure to take an action, unless:

- The director has breached or failed to perform the duties of the director's office in compliance with the duty of care; and

- The breach or failure to perform constitutes willful misconduct or recklessness.

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[12] American Bar Association, Nonprofit Governance and Management, 83 (2002) (citing Daniel L. Kurtz, Board Liabilities: A Guide For Nonprofit Directors, 21 (1988)).

Duty of Loyalty

The duty of loyalty is best described as the expectation that a director will place the interests of the corporation above his or her own personal interests, particularly when the potential for conflict arises. The essence of the duty of loyalty is to recognize and deal appropriately with conflicts. To satisfy the duty of loyalty, a director must avoid conflicts of interests and disclose them when they arise. Additionally, a director may not appropriate to his or her own use a business opportunity that, in fairness, belongs to the organization.

The 1991 Act provides little guidance with respect to handling conflicts of interest and merely provides a safe harbor within which a director's conduct will not render corporate transactions voidable. Thus, to ensure effective enforcement of the duty of loyalty, nonprofit organizations should adopt conflict of interest policies and procedures for their directors and officers.

If properly adopted and administered, a conflict of interest policy can serve several valuable functions for a nonprofit corporation and its directors. The goal of the conflict of interest policy should be full disclosure of any duality of interest or possible conflict of interest that a director may have with respect to the nonprofit corporation. A typical conflict of interest policy will provide for annual disclosure by each director of all business relationships between the director and the organization. The board of directors (or a committee appointed by the board) should compile these disclosure statements and investigate whether a conflict exists. Any director having a business relationship which affects any matter before the organization's board should not vote or use personal influence on the matter. Such interested directors may be counted for purposes of determining whether a quorum exists and may make a presentation at the meeting and answer questions regarding the transaction.

Duty of Obedience

To satisfy the duty of obedience, a director must ensure that the organization complies with all of the rules and regulations to which it is subject. In particular, a director must ensure that the board's decisions further the stated objectives of the organization. Thus, the director should know the rules and abide by them, as well as encourage fellow directors to do the same.

Exposure to Liability

Circumstances giving rise to personal liability of a director or officer can be divided into three broad categories: (1) liability resulting from a breach of fiduciary or statutory duty; (2) liability to third parties for certain acts or omissions of the corporation or of the director or officer acting for the benefit of the corporation; and (3) liabilities occasioned by a violation of federal or state statutes. Potential claimants include the corporation, its members, creditors, the Attorney General, employees, federal or state governmental bodies, and any other aggrieved party with which the organization does business or who is affected by the organization's activities.

Breach of Fiduciary Duty or Statutory Duty

A director, in his or her capacity as a director, may be subject to liability for a breach of any of the duties described above (i.e., duty of care, duty of loyalty, and duty of obedience).

Liability to Third Parties

A director may become liable to third parties under a number of theories, most of which stem from the personal involvement or approval of the director in contributing to some harm caused to a third party. For example, a potential claimant could assert personal liability of a director for contractual torts, patent infringement or any other civil claim that could be made against the organization.

Statutory Liability

Directors are also exposed to liability under a plethora of federal and state statutes, including, among others, federal and state securities laws, federal and state antitrust laws, federal and state tax laws, civil rights legislation and environmental laws.

Tax Withholding and Payroll Taxes

Nonprofit corporations are required to comply with state and federal laws regarding tax withholding and payment of payroll taxes. Directors may be personally liable for any unpaid taxes or penalties if they are found to be "responsible persons" under Code Section 6672. The federal penalty for failure to collect, account for and pay over trust fund taxes is equal to 100% of the trust fund taxes. While Code Section 6672(e) contains an exception for unpaid, voluntary board members of tax-exempt organizations, it is an exception without teeth because it applies only to those directors serving solely in an honorary capacity, who do not participate in the day-to-day or financial operations of the organization,[13] and who do not have actual knowledge of the failure for which such penalty is imposed. Further, the exception does not apply if it results in no person being liable for the penalty.

Protections

Indemnification

The 1991 Act includes a number of provisions related to indemnification of directors and officers. An organization can limit or change such provisions in its Articles of Incorporation. In general, if an individual is made a party to a proceeding[14] because the individual is or was a

[13] See, Thomas v. U.S., 41 F. 3d 1109 (7th Cir. 1994) (where volunteer treasurer and ex-officio chair of finance and planning committee was a responsible person because he had check-signing authority and the opportunity to attend meetings where financial matters were discussed).

[14] A "proceeding" is defined as a threatened, pending or completed action, suit, or proceeding, whether civil, criminal, administrative, or investigative and whether formal or informal under IC 23-17-16-7.

director, a nonprofit corporation may indemnify the individual against liability incurred in the proceeding if:

- The individual's conduct was in good faith; and
- The individual reasonably believed that his or her conduct was in the corporation's best interest.

A nonprofit corporation must indemnify a director against reasonable expenses actually incurred by him or her in connection with a proceeding if the director was wholly successful (on the merits or otherwise) in the defense of a proceeding to which the director was made a party because of his or her role as a director.

A corporation generally may not indemnify a director unless a determination has been made that the director acted in good faith and reasonably believed his or her actions were in the best interests of the organization. The determination must be made by a majority vote of the board of directors, by a committee designated by the board of directors, by special legal counsel or by the organization's members.

As previously discussed, any of the aforementioned provisions can be limited or changed in a corporation's Articles of Incorporation. Furthermore, the indemnification provided under the 1991 Act does not exclude other rights to indemnification that a director may have under the corporation's Articles of Incorporation or Bylaws; a resolution of the board of directors; or any other authorization, adopted after notice, by a majority vote of all of the voting members of the corporation.

Protection for Volunteer Directors

Indiana Code Section 34-30-4-1 provides that "[n]otwithstanding any other law, a qualified director is immune from civil liability arising from the negligent performance of the director's duties." A "qualified director" includes an individual who serves without compensation[15] for personal services as a director or an officer for the purpose of setting policy, controlling, or otherwise overseeing the activities or functional responsibilities of a nonprofit corporation operating, in pertinent part, for charitable, educational, religious, or scientific purposes.[16]

D&O Insurance

The indemnification provisions set forth in the 1991 Act and any indemnification provisions set forth in an organization's Articles of Incorporation offer limited protection to directors. The 1991 Act permits a nonprofit corporation to purchase and maintain insurance on

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[15] IC 34-6-2-28 states that the term compensation for purposes of IC 34-6-2-127 does not include payments to reimburse the expenses of a qualified director or a per diem.

[16] IC 34-6-2-127(2).

behalf of an individual who is or was a director or an officer. Thus, a nonprofit corporation may wish to obtain such insurance to fully cover directors and officers ("D&O Insurance"). D&O Insurance benefits the insured nonprofit entity in many ways, such as:

- Covering the liability of the entity for wrongful acts committed by a director or officer;

- Shifting the burden of defense payments from the entity to the insurance company;

- Limiting the adverse impact of potential D&O liability on a qualified individual's decision to work for or become associated with the nonprofit entity; and

- Facilitating coverage when an entity's public, financial, or political standing would otherwise make direct indemnification of such individuals infeasible.

CHAPTER 6

INDIANA OPEN DOOR LAW

Purpose of the Open Door Law

The intent of Indiana's Open Door Law ("ODL") is that, with few exceptions, all meetings of governing bodies should be open to the public and may be observed and recorded. As a charter school is considered to be a public school and is, therefore, a public agency, most meetings of a charter school board are subject to the ODL.[17] A meeting is defined as a gathering of a majority of the members of the governing body of a charter school for the purpose of taking official action upon public business. The only exceptions to the definition of a public meeting are, in relevant part:

- any social or chance gathering not intended to avoid the law;
- any on-site inspection of any project or program, or facilities of applicants for incentives or assistance from the governing body;
- a gathering to discuss an industrial or a commercial prospect that does not include a conclusion as to recommendations, policy, decisions, or final action on the terms of a request or an offer of public financial resources;
- an orientation of members of the governing body on their role and responsibilities as public officials, but not for any other official action; or
- a gathering for the sole purpose of administering an oath of office to an individual.

"Public business" means any function upon which the board is empowered or authorized to take official action. "Official action" means to receive information, deliberate, make recommendations, establish policy, make decisions; or take final action.

Public Notice

Public notice must be given for all meetings, including executive sessions, at least 48 hours (excluding Saturdays, Sundays, and legal holidays) before the meeting. This notice must contain the date, time and place of the meeting and must be posted at the principal office of the charter school or, if no such office exists, at the building where the meeting is to be held. The notice must also be given to news media organizations (by mail, email or fax) that have filed written requests by January 1 of each year to receive such notices. Notice of regular board

[17] The ODL may be found at IC 5-14-1.5. IC 20-24-4-1(a)(15) requires a charter to specify that the charter school is subject to the requirements of IC 5-14-1.5.

meetings need be given only once each year. Additional notice is required only if there is a change in the normal time, place or date of the regular meeting.

The 48 hour posting and media notification requirements do not apply to a meeting called to deal with an emergency involving actual or threatened danger to person or property. Notice of the meeting must still be posted as soon as possible and news media organizations must be notified at the same time and in the same manner as the members of the body that is meeting. No notice of a properly announced reconvened meeting is required. An agenda cannot be changed and it must be posted at the meeting place.

Agendas and Memorandum

The ODL does not require the use of an agenda. However, if a written agenda is used, it must be posted at the entrance to the location of the meeting prior to the time of the meeting. A meeting notice may be combined with an agenda if it is done timely and posted correctly. Agendas are intended to inform and guide the public and the public officials in the conduct of the meeting.

In addition, a memorandum must be kept at each meeting that includes: the date, time and place of the meeting; the members of the board recorded as present and absent (including those participating via electronic means); the general substance of the matters proposed, discussed or decided; and a record of all votes taken. The memorandum must be available within a reasonable period of time after the meeting for the purpose of informing the public of the proceedings. There is no requirement to keep minutes in addition to the memorandum, but if minutes are kept they must be made available to the public for inspection or copying.

Executive Sessions

The ODL recognizes that in a few circumstances the public may be excluded from a meeting, and the meeting may be conducted as an executive session. An executive session is a meeting from which the public is excluded, except the governing body may admit those persons necessary to carry out its purpose. Executive sessions are permitted only under the following circumstances, in relevant part:

- Where authorized by state or federal law;

- For discussion of strategy necessary for competitive or bargaining reasons with respect to: collective bargaining, the initiation of litigation or of litigation that is either pending or has been threatened specifically in writing, the implementation of security systems, or the purchase or lease of real property (up to the time a contract or option to purchase or lease is executed by the parties);

- To receive information about and interview prospective employees;

- With respect to any individual over whom the governing body has jurisdiction, to receive information concerning the individual's alleged misconduct, and to discuss, prior to any determination, that individual's status as an employee;

- For discussion of records classified as confidential by state or federal statute;

- To discuss before a placement decision, an individual student's abilities, past performance, behavior and needs;

- To discuss a job performance evaluation of individual employees except in the context of the budget process;

- To train school board members with an outside consultant about the performance of the role of the members as public officials; and

- To discuss information and intelligence intended to prevent, mitigate, or respond to the threat of terrorism.

An executive session cannot be conducted during a meeting, and a meeting cannot be recessed in order to meet in executive session and then be reconvened. Furthermore, any final action based on an executive session must still be taken in a meeting open to the public.

Public notice of an executive session must be given in the same manner as notice of a meeting is given, including compliance with the 48 hour posting requirement. However, the notice must also identify the subject matter that is going to be discussed by specific reference to the purpose or purposes for which the executive session is to be held. A memorandum must also be made of an executive session, and it must identify the subject matter considered by specific reference to the instance or instances for which public notice was given. The memorandum (and minutes, if any) must contain a certification by the governing body that no subject matter was discussed in the executive session other than the subject matter specified in the public notice.

Violations and Penalties

Any person may file a law suit to obtain a declaratory judgment, to enjoin continuing, threatened, or future violations of the ODL; or to declare void any policy, decision, or final action: (1) taken at an executive session (where there is no authority for an executive session for that purpose), (2) taken at any meeting for which proper notice was not given, (3) that is based in whole or in part upon official action taken at any unauthorized executive session or meeting for which proper notice was not given; or (4) taken at a meeting held in a location not accessible to persons with disabilities. The person filing the complaint need not allege or prove special damage different from that suffered by the public at large.

Generally, the action must be commenced within 30 days of either the date of the act or failure to act complained of or the date that the person complaining knew or should have known that the act or failure to act complained of had occurred, whichever is later. If a court determines

that a violation has occurred, the court may declare void any policy, decision, or final action taken in violation of the ODL. The court may also enjoin the board from subsequently acting upon the subject matter of the voided act until it has been given substantial reconsideration at a meeting or meetings that comply with the ODL. Furthermore, if the court finds that a violation has occurred, it is required to award reasonable attorney's fees, court costs, and other reasonable expenses of litigation to the person who filed the complaint.

CHAPTER 7

ACCESS TO PUBLIC RECORDS ACT

Purpose of the Access to Public Records Act

The Access to Public Records Act ("APRA") establishes as the State's policy that "all persons are entitled to full and complete information regarding the affairs of government and the official acts of those who represent them as public officials and employees" and that "providing persons with the information is an essential function of a representative government and an integral part of the routine duties of public officials and employees, whose duty it is to provide the information or record." [18] The law defines specific statutory guidelines for maintaining public records and ensuring access to those records by members of the public. Generally, members of the public are entitled to inspect and copy any public record during the regular business hours of a public agency unless there is a specific exception in state or federal law.

Charter School Records

The Indiana Charter School law specifically provides that certain records of a charter school, including records relating to the school's operation and charter and records provided to the DOE or to the sponsor relating to compliance by the organizer with the terms of the charter or applicable state or federal laws, are subject to inspection and copying in accordance with APRA. However, a charter school (and its board) may not disclose the following records:

- records declared confidential by state statute;
- records declared confidential by a rule adopted by a school under specific statutory authority to classify public records as confidential;
- records required to be kept confidential by federal law;
- records containing trade secrets;
- records containing confidential financial information requested from a person;
- records declared confidential by or under the rules of the Indiana supreme court; and
- a Social Security number contained in an otherwise public record.

There are also public records that a charter school and its board may, at its discretion, choose not to disclose, including:

[18] APRA may be found at IC 5-14-3.

- the work product of an attorney who is officially appointed to represent the charter school or its board; however such work product is limited to information compiled by an attorney in reasonable anticipation of litigation;

- test questions, scoring keys and other examination data used in administering an examination for employment, if the examination is to be given again;

- test scores, if the person is identified by name and has not consented to the release of the scores;

- diaries, journals, or personal notes serving as the functional equivalent of a diary or journal;

- records specifically prepared for discussion in an executive session;

- certain personnel records of employees;

- administrative or technical information which, if released, could jeopardize a record-keeping or security system;

- certain computer programs, codes and systems;

- the identity of a donor of a gift under certain conditions; and

- records or parts of records, the public disclosure of which would have a reasonable likelihood of threatening public safety by exposing a vulnerability to a terrorist attack.

Certain personnel information must be released on request and other personnel information can be retained as confidential at the discretion of a charter school or its board. Information that must be provided includes:

- the name, compensation, job title, business address, business telephone number, job description, education and training background, previous work experience, or dates of first and last employment of present or former officers or employees of the school;

- information relating to the status of any formal charges against an employee; and

- the factual basis for a disciplinary action in which final action has been taken and that resulted in the employee being disciplined or discharged.

Records Management

The procedural requirements of APRA necessitate sound records management techniques. In many cases, formal policies will need to be adopted and followed, while in other cases informal procedures will be satisfactory, so long as the personnel responsible for maintaining public records are familiar with those procedures. Charter school officials and board

members have the explicit duty to protect public records from loss or damage. In accomplishing these objectives, a charter school and its board should develop procedures that ensure that individuals who review or copy records do not destroy, mutilate, or remove the record.

Charter school officials and responsible charter school board members must separate disclosable information from the non-disclosable information in a record that contains both. However, a charter school official, board member or employee who unintentionally and unknowingly discloses confidential or erroneous information in response to a public records request or who discloses confidential information in reliance on an advisory opinion by a public access counselor[19] is immune from liability for such a disclosure.

Access Denial Procedure

An individual who wants to inspect a public record must "identify with reasonable particularity" the record requested. Once a public record is requested, a charter school or charter school board must furnish the record unless there is a specific statutory provision prohibiting disclosure or permitting denial. A denial occurs when the person making the request is physically present in the appropriate office, makes the request by telephone, or requests enhanced access to a document and the person designated by the charter school or the charter school board as being responsible for public records release decisions refuses to permit inspection and copying of the record. If a request is made in writing, by facsimile, or through enhanced access, or if an oral request that has been denied is renewed in writing or by facsimile, a charter school or charter school board may deny the request if the denial is in writing or by facsimile and the denial includes a statement of the specific exemption or exemptions authorizing the withholding of all or part of the public record and the name and the title or position of the person responsible for the denial.

Violations and Penalties

A person who has been denied the right to inspect or copy a public record by a charter school or a charter school board may file an action in the circuit or superior court of the county in which the denial occurred to compel the charter school or charter school board to permit the person to inspect and copy the public record. If such an action is filed, the charter school or charter school board is required to notify each person who supplied any part of the public record at issue that a request for release of the public record has been denied and whether the denial was in compliance with an informal inquiry response or advisory opinion of a public access counselor. All of those notified are entitled to intervene in any litigation that results from the denial.

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[19] The office of public access counselor was created in order to provide advice and assistance concerning Indiana's public access laws to members of the public, representatives of the media and government officials and their employees. IC 5-14-4. The counselor may provide written opinions in response to written inquiries, so long as there is no pending administrative or judicial proceeding on the same issue. IC 5-14-5.

The person who has been denied the right to inspect or copy need not allege or prove any special damage different from that suffered by the public at large. This standard of proof is virtually identical to claims for a violation of the ODL. If the person who filed the complaint "substantially" prevails in court, the court is required to award reasonable attorney's fees, court costs, and other reasonable expenses of litigation to the person who filed the complaint. If the charter school or charter school board "substantially" prevails, the court may award reasonable attorney's fees, court costs, and other reasonable expenses of litigation only if the court finds that the action is frivolous and vexatious.

CHAPTER 8

GOOD GOVERNANCE PRACTICES AND FORM 990

In the past decade, both the corporate and nonprofit world have been engaged in an ongoing conversation about the need for better governance practices and enhanced accountability. In 2002, the federal government enacted the Sarbanes-Oxley Act ("SOX") in response to corporate mismanagement controversies such as Enron and WorldCom. Following the enactment of SOX, the discussion about improving corporate management and the need for transparency expanded into the nonprofit world. The Independent Sector's Panel on the Nonprofit Sector embarked on what it described as a thorough examination of the nonprofit sector's governance, transparency, and ethical standards. In 2005, the Panel released its findings in a final report to Congress and the Nonprofit Sector entitled "Strengthening Transparency, Governance, and Accountability of Charitable Organizations."[20] The report recommended more than 120 actions to be taken by charitable organizations, Congress, and the IRS to strengthen the nonprofit sector's transparency, governance, and accountability. After the release of the final report, the IRS responded by redesigning its Form 990 with the stated objectives of enhancing transparency, promoting tax compliance, and minimizing the burden on filing organizations. The end result of this process is that, now more than ever, each charitable organization must be aware not only of the legal *requirements* placed on it, but also of the good governance practices that the IRS and the public expect to see in place.

Sarbanes-Oxley Act

Most of the provisions of SOX are only applicable to the for-profit corporate world, with two exceptions. Code Sections 1102 and 1107 apply to all companies, including nonprofits. Code Section 1102 prohibits persons from document tampering or destruction. Violation of this section could subject the offender to a fine, imprisonment for up to 20 years, or both. Code Section 1107 prohibits retaliation against "whistleblowers" who are providing evidence in relation to a federal offense. A violation of this section could mean a fine, imprisonment for up to 10 years, or both. To ensure compliance with these provisions of SOX, nonprofit organizations should put in place a document retention and destruction policy and a whistleblower policy. Furthermore, those policies should be vigorously followed and enforced.

Form 990

"The Internal Revenue Service believes that a well-governed charity is more likely to obey the tax laws, safeguard charitable assets, and serve charitable interests than one with poor or lax governance."[21] It was on that basis that on December 20, 2007, the IRS released its new

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[20] This report may be found at http://www.nonprofitpanel.org/Report/index.html.

[21] IRS Publication, "Life Cycle of a Nonprofit – Governance and Related Topics" at http://www.irs.gov/pub/irs-tege/governance_practices.pdf, last accessed September, 2011.

version of Form 990, hoping to encourage tax-exempt charities to enact good governance best practices. Because Form 990 is a public document, individuals and companies from whom charities seek funds likely will review a tax-exempt organization's Form 990 before making a gift. So, tax-exempt organizations should view this annual return, which inquires about key governance practices, as an opportunity to show both the IRS and the public (i.e. potential and actual donors) that it is well-governed and successfully serves its stated charitable interests.

Form 990 consists of an 11 page core form, which all tax-exempt charitable organizations are required to complete. There are also 16 schedules that are taxpayer specific. A thoroughly prepared Form 990 will likely include narrative explanations of at least some responses. Each charitable organization should carefully consider who will review its Form 990. In fact, one of the questions on the Form 990 asks whether the organization provides a copy of Form 990 to its governing body, and requires the organization to explain any process of review by its directors or management.

Good Governance Practices

Addressing Governance Issues

Nonprofit organizations should be proactive in addressing and adopting the good governance practices emphasized in the Form 990. Boards need to recognize that improved governance means improved prospects for the organization's future.

Governance related issues can be difficult to discuss in a board setting. If, as a board member you are leading a governance review, you must create a safe, productive environment in which authentic conversations about governance can take place. Start by reviewing the organization's current governing documents (Articles of Incorporation, Bylaws, and any amendments to those documents). In this review, determine if the organization is organized and operated under the most recent version of the relevant nonprofit statute (for example, the 1991 Act in Indiana). In particular, review these documents to determine if the organization's directors and officers are afforded the maximum indemnity protections afforded by the current law. If directors and officers are not so protected, revise the governing documents accordingly. In addition, a governance review may examine a tax-exempt organization's purpose and mission; governing body; financial statements and financial oversight; transparency and accountability; and corporate policies.[22]

Purpose and Mission

An organization's purpose and mission will be stated on the first page of the Form 990, so it is particularly important that it reflect the organization's activities. The purpose and mission

[22] One good resource guide to the review process is published by the Independent Sector, titled "Principles Workbook: Steering your Board Toward Good Governance and Ethical Practice." This workbook is available online at http://www.nonprofitpanel.org.

should explain why the organization exists, what it hopes to accomplish, and what activities it will undertake.

Governing Body

Ideally, every tax-exempt organization will have a governing body that is active and engaged, with members who are selected with the charity's needs in mind. Also, the size of the board of directors should be an appropriate size to govern your particular organization. If, upon review, you find that any of these things are not true of your board, the board should consider measures to re-engage its members, add members with particular skills, or change the size of the board, as necessary.

The IRS has stated that it will review the board composition to determine if the board represents a broad public interest, and to identify the potential for insider transactions that could result in misuse of charitable assets. It wants to see a board with a majority of its voting members independent of the tax-exempt organization.

Furthermore, since the board of directors will probably not be completely "independent," it is important to manage any conflicts of interest of board members by adopting a conflict of interest policy. Conflict of interest policies are fairly standard in nonprofit organizations and are vital to sound stewardship practices. The policy should be detailed and drafted in accordance with the operation of a nonprofit organization. In particular, a sound conflict of interest policy should acknowledge that a nonprofit organization may seek to recruit and retain board members who, under a strict definition of "conflict," have conflicts because they are established individuals with many community connections. Therefore, conflict avoidance should not be the policy, but rather ethical conflict management and an overarching requirement that in all situations in which a conflict is present, a director's duty of loyalty runs to the nonprofit organization.

Financial Statements and Financial Oversight

The board (or a board authorized committee) is responsible for the review and oversight of a tax-exempt organization's financial resources. As part of a governance review, the board should ask the following questions: Does the organization have an audit committee? Is the audit committee independent? Is someone on the audit committee a "financial expert"? Can the audit committee hire and fire the auditor? Is the outside auditor independent? If the answer to any of these questions is "no," the board should consider making changes.

Transparency and Accountability

The board should consider what documents it is making public, and the methods it is using to provide public access to those documents. The IRS recommends that a tax-exempt organization publish annual reports, financial statements, governing documents, and a conflict of interest policy on the organization's website. An organization is also required to disclose and make available for public inspection its Form 1023, its Form 990, and its Form 990-T (unrelated business income tax return).

Written Policies

A governance review should also consider what board policies are appropriate or necessary. Form 990 affirmatively asks whether your board of directors has adopted a number of written policies including three we have already discussed (the conflict of interest policy, the whistleblower policy, and the document retention and destruction policy) and four additional policies: an executive compensation policy; a joint ventures policy (if the organization participates in joint venture arrangements); an expense reimbursement policy (specifically addressing certain luxury services); and a gift acceptance policy. The IRS does not have the authority to mandate that an organization adopt these written policies. However, responding on Form 990 that an organization does not have these written policies could increase an organization's IRS audit risk and could be perceived negatively by the general public as they review the organization's Form 990.

Connect the Dots

More and more is being asked of nonprofit boards. Therefore, as a leader of a nonprofit charter school, you must ensure that any governance review project has a tangible and appropriate end. If your organization is anticipating a capital campaign, or an endowment drive, or a leadership transition, or a change in focus, incorporate a governance review into the early planning stages of such efforts. This will accommodate reform but also tie the reform to a greater purpose that your board can grasp and about which it can get excited.

CHAPTER 9

INTERMEDIATE SANCTIONS REGULATIONS

In the past, if a tax-exempt organization violated the prohibitions against private inurement, the IRS' only tool was to revoke the organization's tax exemption. Now, intermediate sanctions legislation gives the IRS an alternative to revocation and permits it instead to impose an excise (or penalty) tax upon the organization and, in some instances, its managers. Code Section 4958 imposes a tax on any disqualified person who engages in an excess benefit transaction with specified organizations.

Applicability and Definitions

These rules only apply to transactions between certain tax-exempt organizations (e.g., organizations described in Code Sections 501(c)(3) or 501(c)(4)) and a disqualified person. A disqualified person is a person who is or has been in a position to exercise substantial influence over the affairs of the organization during the five years ending on the date of the transaction, a member of his or her family, or an entity in which the disqualified person has control in excess of 35% percent. Certain persons are deemed to be in a position to exercise substantial control over an organization, i.e., voting members of the governing body, the president, the chief executive officer, the chief operating officer, the treasurer and the chief financial officer. Others may be in a position to exercise substantial control over the organization if the facts and circumstances justify such a conclusion.

The excess benefit is the amount by which the value of the economic benefit provided by the organization directly or indirectly to or for the use of a disqualified person exceeds the consideration received from the disqualified person. Therefore, an excess benefit transaction occurs when an economic benefit is provided by the organization directly or indirectly to or for the use of any disqualified person and the value of the economic benefit provided exceeds the value of the consideration, including services, received for providing such benefit. The IRS will treat the transaction as an "automatic" excess benefit transaction unless the exempt organization clearly indicates in writing, contemporaneous to the payment of the economic benefits, that such payments were to be treated as compensation for services provided.

Rebuttable Presumption

Treasury Regulations issued by the IRS allow an organization to establish a rebuttable presumption that a transaction is not an excess benefit transaction by complying with the following procedures:

- The transaction must be approved in advance by the organization's board, a committee of the board, or other parties authorized by the board to act on its behalf (to the extent permitted by state law) composed entirely of individuals who do not have a conflict of interest with respect to the transaction.

- The approving body must obtain and rely upon appropriate data as to the comparability of the terms of the transaction prior to making its decision. The approving body has appropriate comparability data if, considering the knowledge and expertise of its members, it has sufficient information to determine that the transaction in its entirety is reasonable or at fair market value.

- The approving body must adequately document the basis for its determination concurrently with making that decision. Adequate documentation must include information such as the terms of the transaction, the date of approval, the comparability data obtained and relied upon, and any actions taken by anyone on the approving body who had a conflict of interest with respect to the transaction.

Excise Tax on Disqualified Persons

Code Section 4958 imposes a tax at an initial rate of 25% on a disqualified person who receives an excess benefit from an organization. An additional tax at a rate of 200% will be imposed if the excess benefit is not timely corrected.

The IRS may abate the 200% tax even after the taxable period if the excess benefit transaction is corrected within a subsequent ninety-day correction period. In order to correct the excess benefit transaction, the disqualified person must undo the excess benefit and take any other steps necessary to return the organization to a financial position not worse than that in which it would be if the disqualified person were dealing under the highest fiduciary standards. The disqualified person should make a payment to the organization, in cash or cash equivalent, equal to the excess benefit and any interest on such benefit. A promissory note does not suffice. Alternatively, the disqualified person may return to the organization specific property which was the subject of the excess benefit transaction. Such a return of property will be treated as a payment in an amount equal to the lesser of the fair market value of the property: (1) on the date returned, or (2) on the date of the excess benefit transaction. Any agreement underlying the excess benefit transaction need not be rescinded; however, an ongoing agreement must be modified as necessary to prevent any future excess benefit transactions.

Excise Tax on Organization Managers

In addition, an organization manager who participates in an excess benefit transaction may be taxed at a rate of 10% of the excess benefit up to a limit of $20,000 per transaction. The manager must participate knowingly and willingly, and his or her participation must not be due to reasonable cause. An organization manager is any officer, director or trustee of an organization, or any person having powers and duties similar to such positions. Participation includes inaction where the manager is under a duty to speak. A manager has not participated where the manager opposes the transaction in a manner which is consistent with the fulfillment of the manager's duties to the organization. A manager's participation is willful if it is voluntary, conscious and intentional. A manager's participation is due to reasonable cause if the manager has acted with ordinary business care and prudence.

The manager's participation will be considered knowing if the manager: (1) has actual knowledge of sufficient facts to establish that the transaction is an excess benefit transaction; (2) is aware that the transaction may violate the provisions of Code Section 4958; and (3) is aware that it is an excess benefit transaction or negligently fails to attempt to determine whether it is an excess benefit transaction. Having reason to know is not sufficient to establish that the manager knowingly participated but will be considered together with all other applicable facts and circumstances. An organization manager will not be deemed to knowingly participate if the manager has fully disclosed the applicable facts to an appropriate professional and thereafter relied upon a reasoned written opinion issued by the professional with respect to the portions of the transaction within the professional's area of expertise. Appropriate professionals may include legal counsel, CPAs and certain valuation experts.

Special Rule for Initial Contracts

Code Section 4958 does not generally apply to certain fixed payments made pursuant to an initial (or new) contract. A fixed payment is a payment the amount of which is specified in a contract or determined by a fixed formula specified in a contract. This exception applies only if the person substantially performs pursuant to the initial contract. An existing written binding contract is treated as a new contract under certain circumstances, such as if the contract is materially changed. The application of this exception can be confusing. Therefore, if your organization believes it has a qualifying initial contract, a legal advisor should be consulted before making a determination that the exception applies.

CHAPTER 10

TAXATION OF UNRELATED BUSINESS INCOME

Income of a tax-exempt organization is typically exempt from federal taxation to the extent that the income is generated from an activity that is related to the basis of the organization's tax-exemption. For unrelated business taxable income ("UBTI") of Code Section 501(c)(3) organizations, Code Section 511 imposes an unrelated business income tax ("UBIT"). UBIT is computed as provided in Code Section 511 (i.e., by applying the corporate tax rates to the amount of UBTI received by the organization). When enacting UBIT, the legislature's primary objective was to eliminate unfair competition by placing a tax-exempt organization's unrelated business activities on the same tax footing as its taxable competitors. The statute was specifically intended to remedy perceived abuses of the tax laws by tax-exempt organizations that operated full-fledged commercial enterprises in direct competition with fully taxable organizations. In addition to the application of a high rate of tax on such income, an organization can endanger its tax-exempt status if the unrelated business activity becomes a predominant activity of the organization.

Defining Unrelated Business Taxable Income

Code Section 512(a)(1) defines the term "unrelated business taxable income" to include "the gross income derived by any organization from any unrelated trade or business (as defined in Code Section 513) regularly carried on by it." Code Section 513(a) defines the term "unrelated trade or business" to include "any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational or other purpose or function constituting the basis for its exemption under Section 501." Treasury Regulation § 1.513-1 explains the above requirements with respect to UBTI treatment.

The Business Activity Must Qualify as a Trade or Business

A tax-exempt organization that engages in a trade or business which is not substantially related to its exempt purpose will not enjoy the benefits of its tax exemption with respect to these activities. For purposes of UBIT, the term "trade or business" will have the same meaning as in Code Section 162 and will, therefore, generally include any activity carried on for the production of income from the sale of goods or performance of services. Furthermore, many courts have adopted the "profit motive" test in identifying a trade or business and look to whether the activity was "entered into with the dominant hope and intent of realizing a profit."[23]

[23] U.S. v. American Bar Endowment et al., 477 U.S. 105 (1986) (tax-exempt organization that raised money for charitable work by providing insurance policies to members was subject to UBIT because it exhibited characteristics of trade or business and engaged in sale of goods and performance of services).

The Trade or Business Must Be "Regularly Carried On"

Additionally, the tax-exempt organization must "regularly carry on" the trade or business. The following factors are considered in determining whether a trade or business is "regularly carried on": (1) the frequency of the activities; (2) the continuity of the activities; and (3) the manner in which the activities are carried on. Specifically, in evaluating whether an activity is "regularly carried on," the IRS will apply these three factors and compare the conduct of the exempt organization to the manner in which similar commercial activities are pursued by taxable organizations.

The Activity Is Not "Substantially Related" to the Organization's Exempt Purpose

Lastly, if an organization's activity has met the previous two requirements and if the activity is not "substantially related" to its exempt purpose, the organization will be subject to UBIT. This determination involves an examination of the relationship between the activity undertaken and the accomplishment of the organization's exempt purposes. A trade or business is "related" to exempt purposes if the conduct of the business activity has a causal relationship to the achievement of an exempt purpose (other than through the production of income). It is "substantially related" for purposes of Code Section 513 as long as the causal relationship is a "substantial one." The conduct of a trade or business will be "substantially related" to the organization's exempt purposes, for which it received its exemption under Code Section 501(c), if the production or distribution of goods or the performance of the services, from which the gross income is derived, contribute importantly to the accomplishment of the exempt purposes of the organization.

The "substantially related" requirement is met where the size and extent of the business are justified given the nature and extent of the exempt function which they purport to serve. Where income is realized by a tax-exempt organization partly in consideration for the performance of its exempt purposes but the activities are conducted on a larger scale than is reasonably necessary for the performance of such functions, the gross income attributable to the excess activities is subject to UBIT.

Exceptions to UBTI

Under Code Section 512(b) and the corresponding Treasury Regulations, the following types of income (and deductions directly connected with such income) are generally excluded when calculating UBTI:

Dividends, Interest, Annuities, and Other Investment Income

All dividends, interest, annuities, payments received from a securities loan, and other income that is substantially similar to an exempt organization's ordinary and routine investments are excluded in computing UBTI. However, this exclusion does not apply to: (1) certain insurance activities of an exempt organization's controlled foreign corporation; (2) unrelated debt-financed income; or (3) interest or annuities received from a controlled corporation.

Royalties

In general, royalties are excluded in computing UBTI. Payments that relate to the use of a valuable right will be considered royalties. The following payments cannot be excluded as royalties: (1) payments for personal services; (2) payments for personal appearances and interviews; (3) income from mineral rights where an organization is not relieved of its share of the development costs; and (4) income from unrelated debt-financing.

Rents

In general, rents are excluded in computing UBTI. All rents from real property are excluded, unless substantial services are rendered to the tenant as well. Rents from personal property are excluded if the personal property is leased in conjunction with real property and the rents attributable to personal property are incidental to the amount of total rents received under the lease. However, if more than 50% of the total rents are attributable to personal property or the determination of the rent depends in whole or in part on the income or profits from the leased property, the rents cannot be excluded.

Income From Research

In general, tax-exempt organizations may exclude income from research grants or contracts in computing UBTI. Income from research will be excluded in the following circumstances: (1) income derived from research for the United States (or any of its agencies or instrumentalities), any State or political subdivision thereof; (2) income derived from research performed for any person at a college, university, or hospital; and (3) income derived from research by an organization operated primarily for the purpose of carrying on fundamental research where the results of the research are freely available to the general public. The term "fundamental research" does not include activities normally carried on primarily for commercial or industrial application.

Gains and Losses From Dispositions of Property

In general, a tax-exempt organization may exclude from UBTI, any gains or losses from the sale, exchange, or other disposition of property. However, income from the following dispositions of property may not be excluded from UBTI: (1) stock in trade or other property of a kind that would properly be included in inventory if on hand at the close of the tax year; (2) property held primarily for sale to customers in the ordinary course of a trade or business; and (3) cutting of timber that an organization has elected to consider as a sale or exchange of timber.

CHAPTER 11

SUBSTANTIATION AND DISCLOSURE REQUIREMENTS FOR DONATIONS

Substantiation Requirements

Written Acknowledgement

A donor cannot claim a tax deduction for any single contribution of $250 or more unless the donor substantiates the contribution with a contemporaneous, written acknowledgement of the contribution from the recipient organization (i.e., the donee). A written acknowledgement is contemporaneous if it is obtained by the donor on or before the earlier of: (1) the date the taxpayer files the original return for the taxable year in which the contribution was made, or (2) the due date (including extensions) for filing the taxpayer's original return for that year. Under Treasury Regulation § 1.170A-13(f), the written acknowledgement from the donee organization must contain the following information:

- The name of the donee organization;
- The amount of any cash the donor paid and a description (but not necessarily the value) of any property other than cash the donor transferred to the donee organization;
- A statement of whether the donee organization provided any goods or services in consideration, in whole or in part, for any of the cash or other property transferred to the donee organization;
- If the donee organization provided any goods or services other than intangible religious benefits, a description and good faith estimate of the value of those goods or services; and
- If the donee organization provided any intangible religious benefits, a statement to that effect.

The IRS does not provide or require a specific form for the acknowledgement. It may be handwritten, computer generated or transmitted to the donor via e-mail. Attached as Exhibit 1 is a sample written acknowledgement.

Goods or Services Provided

The acknowledgement must describe goods or services a donee organization provides in exchange for a contribution of $250 or more. It must also provide a good faith estimate of the value of such goods or services because a donor must generally reduce the amount of the contribution deduction by the fair market value of the goods and services provided by the donee.

Goods or services include cash, property, services, benefits or privileges. However, certain goods and services do not need to be described in an acknowledgement, such as: (1) insubstantial goods or services that a donee provides in exchange for contributions; (2) an insubstantial annual membership benefit; and (3) intangible religious benefits provided by a religious organization to a donor.

Payroll Deductions

When a donor makes a single contribution of $250 or more by payroll deduction, the donor may use the following documents as the written acknowledgement: (1) a pay stub, Form W-2 or other document furnished by the employer that sets forth the amount withheld by the employer and paid to a charitable organization; and (2) a pledge card that includes a statement to the effect that the organization does not provide goods or services in consideration for contributions to the organization by payroll deduction.

Unreimbursed Expenses

A taxpayer who incurs unreimbursed expenditures while providing services to a tax-exempt organization may deduct the value of these expenses. The taxpayer may substantiate the deduction if the taxpayer: (1) has adequate records to substantiate the amount of the expenditures (such as receipts, cancelled checks, and mileage logs); (2) obtains a statement from the donee organization that describes the services provided by the taxpayer and whether the donee organization provided any goods or services in consideration for the unreimbursed expenditures; and (3) describes whether the donee organization provided any goods or service other than intangible religious benefits and, if so, a statement to that effect.

Quid Pro Quo Disclosure Rules

A donor may only take a charitable contribution deduction to the extent that the contribution exceeds the fair market value of the goods or services the donor receives in return for the contribution. A contribution made in exchange for goods or services is known as a "quid pro quo" contribution. A donee must provide a written disclosure statement to a donor who makes a payment exceeding $75 partly as a contribution and partly in exchange for goods and services provided by the organization.

This written disclosure statement must: (1) inform the donor that the amount of the contribution that is deductible for federal income tax purposes is limited to the excess of cash (and the fair market value of property other than cash) contributed by the donor over the value of the goods or services provided by the donee, and (2) provide the donor with a good faith estimate of the fair market value of the goods or services that the donee provided in return. A donee must furnish a disclosure statement in connection with either the solicitation or the receipt of the quid pro quo contribution. The statement must be in writing and must be made in a manner that is likely to come to the attention of the donor. Enclosed as Exhibit 2 is a sample quid pro quo acknowledgment letter. An organization that does not provide a written disclosure statement when required may incur a $10 penalty per contribution, with a maximum penalty of $5,000 per fundraising event or mailing.

CHAPTER 12

INDIANA PROFESSIONAL FUNDRAISING AND CHARITABLE SOLICITATION REGULATION

The Professional Fundraiser Consultant and Solicitor Registration Act (the "Act"), codified in Indiana Code Section 23-7-8-1, *et. seq.*, regulates the registration and actions of fundraising consultants and solicitors who seek, for a fee, contributions for charitable organizations in Indiana.[24]

Definitions

A "professional fundraiser consultant" under the Act is any person[25] who is hired for a fee to plan, manage, advise or act as a consultant in connection with soliciting contributions for or on behalf of a charitable organization, but who does not actually solicit contributions as a part of the person's services or employ, procure, or engage a compensated person to solicit contributions. A "professional solicitor" under the Act is a person who, for financial consideration, solicits contributions for or on behalf of a charitable organization, either personally or through agents or employees specifically employed for that purpose. A charitable organization or a bona fide officer, employee, member or volunteer of a charitable organization that solicits on behalf of the organization is not considered a professional fundraiser consultant or professional solicitor for purposes of the Act.

The term "contribution" means a promise or pledge of money, a payment or any other rendition of property or service. It does not include membership dues, fines or assessments, nor payments for property sold or services rendered by the organization (if not sold or rendered in connection with a solicitation). A solicitation is: (1) a request for financial assistance in any form on the representation that such assistance will be used for a charitable purpose, or (2) selling, offering or attempting to sell any advertisement, advertising space, membership or tangible item in certain circumstances. A solicitation is considered to have taken place under the Act even if the person making the solicitation does not receive a contribution.

Requirements for Action as a Professional Fundraiser Consultant or Solicitor

Registration

In order to act as a professional fundraiser consultant or solicitor, a person must first register with the Consumer Protection Division of the Office of the Attorney General (the

[24] More information, including the various forms, notices and reports mentioned in this Chapter may be found on the website of the Indiana Attorney General at http://www.in.gov/attorneygeneral/2379.htm.

[25] For purposes of the Act, the term "person" includes any individual, organization, trust, foundation, association, partnership, limited liability company or corporation.

"Division"). Certain information is required to apply for registration, such as the names and addresses of all officers, employees and agents who are actively involved in fundraising, the names and addresses of all persons who own a 10% or greater interest in the registrant, and the name under which the registrant intends to solicit contributions.

Contracts with Charitable Organizations

Before acting as a professional fundraiser consultant for a particular charitable organization, the consultant must enter into a written contract with that organization identifying the services that the consultant is to provide and stating whether the consultant will have custody of the contributions at any time. This contract must be filed with the Division. A professional solicitor is also required to enter into a contract before engaging in charitable solicitations. The solicitation contract must specify the percentage of gross contributions the charitable organization is to receive or the terms upon which such a determination is to be made. The amount the charitable organization is to receive must be expressed as a fixed percentage of the gross revenue or a reasonable estimate of the gross revenue. This figure must exclude, however, any amount that the charitable organization is required to pay as expenses of the solicitation campaign, including the cost of any merchandise or services sold. The contract must also disclose the average percentage of gross contributions received by charitable organizations collected on their behalf by the professional solicitor for the three year period preceding the year in which the contract was made.

Information Required for Solicitation Campaigns

A professional solicitor must file a solicitation notice with the Division before beginning a solicitation campaign. This notice must contain a copy of the solicitation contract described above, the projected beginning and end dates of the campaign, and the names and addresses of persons responsible for the direction and supervision of the conduct of the campaign. After the solicitation campaign has been completed, the solicitor must inform the Division of the amount of money it collected, the amount paid to the professional solicitor, the amount paid by the charitable organization as expenses of the campaign, and the total amount of money received by the charitable organization.

Fees

The initial fee to register as a professional fundraiser consultant or solicitor is $1,000. A partnership, limited liability company, corporation or other entity that intends to act as a professional fundraising consultant or solicitor may pay a single $1,000 on behalf of all of its members, agents, officers and employees. The registration must be updated annually and a renewal fee of $50 is assessed at that time.

Disclosures Required of Professional Solicitors

Under the Act, a professional solicitor is required to make certain disclosures at the time the solicitation is made and before the donor agrees to make a contribution. These disclosures must be clear and conspicuous and must be in writing if the solicitation is being made in writing.

Oral disclosures are required if the solicitation is being made by telephone. These disclosures include:

- the name and, upon request, the address of the charitable organization being represented;
- the fact that the person soliciting the contribution is, or is employed by, a professional solicitor and is compensated;
- the full name of the professional solicitor and, upon request, the telephone number that the person being solicited can call to confirm the information being provided; and
- the charitable purpose for which the funds are being raised.

Upon receiving a contribution, the professional solicitor must mail a written confirmation of the contribution within 10 days. This confirmation also must contain the name and, upon request, the address of the charitable organization being represented and the disclosure that the person soliciting the contribution is a professional solicitor.

Right to Cancel Pledge

A contributor has the right to cancel a pledge for a contribution at any time prior to actually making the contribution.

Prohibited Practices

A professional solicitor may not engage in the following prohibited practices:

- representing registration by the state as an endorsement by the state;
- misrepresenting that the person is an officer or employee of a public safety agency;
- use of the name "police," "law enforcement," "trooper," "rescue squad," "fireman," or "firefighter" unless a bona fide police, law enforcement, rescue squad, or fire department authorizes its use in writing;
- misrepresenting to anyone that the contribution will be used for a charitable purpose if the professional solicitor has reason to believe that it will not be;
- misrepresenting that another person endorses the solicitation unless that person has given written consent for the use of his or her name to endorse the solicitation;
- misrepresent to anyone that the contribution is being solicited on behalf of anyone other than the charitable organization that authorized the solicitation;

- collect or attempt to collect a contribution in person or by means of a courier unless the solicitation is made in person and the collection or attempted collection is made at the time of the solicitation, or the contributor has agreed to purchase goods in connection with the solicitation and the collection is made or attempted at the time of the delivery of the goods; or

- representing that tickets to events will be donated for use by another unless the solicitor has written commitments from charitable organizations stating that they will accept a specific number of donated tickets. The solicitor may not solicit contributions for more donated tickets than the number of ticket commitments received from charitable organizations.

Fundraising and Solicitation Laws of Other States

A majority of states have adopted comprehensive charitable solicitation acts to assist with the regulation of fundraising for charitable organizations and professional fundraisers and solicitors. These charitable solicitation laws can be quite diverse, making generalizations regarding the requirements, limitations and prohibitions on charitable fundraising a hazardous undertaking for organizations subject to regulation in states other than Indiana. An organization that will itself solicit contributions or solicit contributions through the use of a professional fundraiser or solicitor in another state should consult with legal counsel to ensure that it is in compliance with the other state's laws. In some states, failure to comply with the fundraising or solicitation statutes could result in a felony. Organizations must also be aware that cities, counties and towns may have solicitation ordinances or rules that must be taken into account before soliciting contributions.

CHAPTER 13

PROPERTY TAX EXEMPTION

Except as expressly provided by law, all real and business tangible personal property in Indiana is annually subject to assessment and taxation for *ad valorem* property tax purposes. The Indiana Constitution authorizes the General Assembly to exempt from property tax all property "being used for municipal, educational, literary, scientific, religious or charitable purposes." In response, the Indiana legislature has enacted a number of property tax exemptions for uses that advance general social policies. The exemptions are all provided by statute, and the procedures required to obtain the exemption must be strictly followed.

The "General Charitable Exemption" Statute

There are several specific statutory exemptions (including for example, exemption of certain properties owned by governmental entities, churches and religious societies, fraternal organizations, nonprofit corporations promoting the fine arts, public libraries, etc.), which are beyond the scope of this handbook. The exemption most commonly applicable to charter school organizers is the "general charitable exemption statute" set forth in Indiana Code Section 6-1.1-10-16. The basic requirements of the general charitable exemption statute are as follows.

Owned, Occupied, And Used

All or part of a building is exempt from property taxation if it is owned, occupied and used by a person for educational, literary, scientific, religious, or charitable purposes. A tract of land is exempt if it (a) holds a building or a parking lot or structure that serves a building used for exempt purposes; or (b) is owned by a nonprofit entity established to retain and preserve land and water for their natural characteristics, provided it is no more than 500 acres and the entity does not use the land for profit. Personal property is exempt if it is owned and used in such a manner that it would be exempt if it were a building.

What Is "Charitable"

A charitable purpose will be found to exist if there is evidence of relief of human want manifested by obviously charitable acts different from the everyday purposes and activities of man in general and there is an expectation that a benefit will inure to the general public sufficient to justify the loss of tax revenue. The concept includes lessening the burdens of government.

What Is "Educational"

The test that the Indiana Courts have historically applied is whether the property is used to relieve the State's burden of providing education, to some limited extent, by providing courses that are at least related to those found in tax-supported schools. Most, if not all, charter schools should satisfy this test.

Property Tax Exemption Procedures

An exemption is a privilege which may be waived. If an owner does not comply with the statutory procedures for claiming the exemption, the exemption is waived and the property is taxable. The general procedures for claiming exemption from property tax are codified in Indiana Code Section 6-1.1-11 and apply unless other procedures for obtaining a specific exemption are specially provided.

General Filing Requirements

Generally, an owner of tangible property that wishes to obtain an exemption must file Form 136, *Application for Property Tax Exemption*, in duplicate with the county assessor of the county in which the property is located. The application is required to contain a description of the property, a statement showing the ownership, possession, and use of the property, the grounds for exemption, the name and address of applicant, an identification of "each part" of the property used or occupied (and each part not used or occupied) for exempt purposes, and anything else required by the Department of Local Government Finance ("DLGF"). The application must be filed on or before May 15 of the year for which exemption is claimed. If an exemption is required to be claimed on or in an application accompanying a personal property tax return, it can be filed on or with a return up to 30 days after the filing date for the return.

Frequency of Filing

In general, a nonprofit corporation seeking exemption under the general charitable exemption statute for property directly owned by the nonprofit corporation in an even-numbered year must file Form 136 in that year. A nonprofit corporation is not required to file an exemption application in an odd numbered year if: (a) it received an exemption in the immediately preceding year; and (b) the property's use has remained unchanged. A nonprofit corporation must file an exemption application in an odd numbered year (or any year for that matter) if exemption is desired for property that was not exempted in the previous year.

The 2009 budget bill modified the general rule by providing, among other things, that a nonprofit corporation owning property recognized as exempt in 2009 under the general charitable exemption statute (Indiana Code Section 6-1.1-10-16) need not file an application for that property in 2010 or ever again if: (1) the property continues to meet the appropriate statutory exemption requirements; and (2) an exemption application was properly filed at least once. This is a relatively new and narrow exception that should be considered carefully with tax counsel before pursuing a course of not filing for exemption.

Failure To Timely File

The failure to timely claim an exemption waives the exemption. Directors of nonprofit organizations who may be eligible for property tax exemption should take care to ensure deadline are met. In addition, nonprofit organizations should seriously consider consulting counsel for assistance in the exemption process because qualification for exemption often presents complex legal questions and the procedures are full of traps for the unwary.

CONCLUSION

As you can see, the requirements and limitations applicable to a nonprofit, tax-exempt charter school are extensive and often quite detailed. Please don't let that discourage you from serving as a board member for one or more of the many worthwhile schools that currently exist or which are in the process of opening in Indiana. As a board member, it is not necessary that you have a detailed understanding of each of these requirements and restrictions. However, it is important that you have a general understanding of the issues covered in this Handbook so that you are able to spot potential issues and identify the need for additional guidance and counsel. It is our hope that this guide has assisted you in gaining a basic understanding which will permit you to be a productive and responsible board member. Together, we can help Indiana's charter school sector continue to grow and flourish.

APPENDIX A

STATE STATUTES APPLICABLE TO CHARTER SCHOOLS[26]

1) IC 5-11-1-9 (required audits by the state board of accounts).
2) IC 20-39-1-1 (unified accounting system).
3) IC 20-35 (special education).
4) IC 20-26-5-10 (criminal history).
5) IC 20-26-5-6 (subject to laws requiring regulation by state agencies).
6) IC 20-28-10-12 (nondiscrimination for teacher marital status).
7) IC 20-28-10-14 (teacher freedom of association).
8) IC 20-28-10-17 (school counselor immunity).
9) IC 20-33-2 (compulsory school attendance).
10) IC 20-33-3 (limitations on employment of children).
11) IC 20-33-8-19, IC 20-33-8-21, and IC 20-33-8-22 (student due process and judicial review).
12) IC 20-33-8-16 (firearms and deadly weapons).
13) IC 20-34-3 (health and safety measures).
14) IC 20-33-9 (reporting of student violations of law).
15) IC 20-30-3-2 and IC 20-30-3-4 (patriotic commemorative observances).
16) IC 20-31-3, IC 20-32-4, IC 20-32-5, IC 20-32-6, IC 20-32-8, or any other statute, rule, or guideline related to standardized testing (assessment programs, including remediation under the assessment programs).
17) IC 20-33-7 (parental access to education records).
18) IC 20-31 (accountability for school performance and improvement).
19) IC 20-30-5-19 (personal financial responsibility instruction).

[26] IC 20-24-8-5. In addition to the above, conversion charter schools are subject to: IC 20-28-6 (teachers contracts), IC 20-28-7.5 (cancellation of teachers contracts), IC 20-28-8 (contracts with school administrators), IC 20-28-9 (salary and related payments), and IC 20-28-10 (conditions of employment).

APPENDIX B

SELECTED RESOURCES

Applicable Indiana Statutes

Indiana Charter School Law
http://www.in.gov/legislative/ic/code/title20/ar24/

Access to Public Records Act
http://www.in.gov/legislative/ic/code/title5/ar14/ch3.html

Indiana Open Door Law
http://www.in.gov/legislative/ic/2010/title5/ar14/ch1.5.html

Sponsors and Regulators

Ball State University Office of Charter Schools
http://www.bsu.edu/teachers/charter/

Indiana Charter School Board
http://www.doe.in.gov/CharterBoard/

Indianapolis Office of Education Innovation
http://www.indy.gov/eGov/Mayor/programs/education/Charter/Pages/home.aspx

Indiana Public Access Counselor
http://www.in.gov/pac/

Internal Revenue Service
http://www.irs.gov/charities/

Indiana Secretary of State
http://www.in.gov/sos/

Indiana Department of Revenue
http://www.in.gov/dor/

Industry Links

Indiana Public Charter Schools Association
http://www.incharters.org/

National Association of Charter School Authorizers
http://www.qualitycharters.org/index.php

EXHIBIT 1

SAMPLE DONOR ACKNOWLEDGEMENT LETTER

ABC, Inc.
123 Anywhere Lane
Somewhereville, Anystate 12345

[Date]

Ms. Jane Doe
987 Main Street
Anywhere, Anystate 12345

Dear Ms. Doe:

We would like to thank you for your contribution of $250 **[or provide a description, but no value, of any in-kind contribution - e.g., ten dance costumes]** made on _____. ABC, Inc. did not provide any goods or services in consideration, in whole or in part, for your contribution.

Thank you again for your contribution.

Sincerely,

Jonathan Doe
Secretary

EXHIBIT 2

SAMPLE QUID PRO QUO DONOR ACKNOWLEDGEMENT LETTER

ABC, Inc.
123 Anywhere Lane
Anywhere, Anystate 12345

[Date]

Ms. Jane Doe
987 Main Street
Anywhere, Anystate 12345

Dear Ms. Doe:

We would like to thank you for your contribution of $100 made on _____. In connection with your contribution, ABC, Inc. provided a dinner to you.

Please note that, pursuant to Section 6115 of the Internal Revenue Code of 1986, as amended, the amount of your contribution that is deductible as a charitable contribution deduction for federal income tax purposes is limited to the excess of the amount of any money **[and the value of any property other than money]** which you contributed over the value of the goods or services which we provided to you. **[We cannot estimate for you the value of any property you contributed. You must determine that on your own.]** However, we have made a good faith estimate that the fair market value of the goods and services which we provided for your benefit is **[$_____]**.

Thank you again for your contribution.

Sincerely,

Jonathan Doe
Secretary